THE NEW REALITY OF RISING PENSION COSTS

CCLC ANNUAL CONFERENCE · November 16, 2018

INTRODUCTIONS

- **LIZETTE NAVARETTE**
  Vice President at Community College League of California

- **MAUREEN TOAL**
  Senior Vice President at Public Agency Retirement Services (PARS)

- **JOSE TORRES**
  Executive Vice Chancellor at San Bernardino Community College District

- **DAN TROY**
  Assistant Superintendent/Vice President Administrative Services at Cuesta College

Strategies for Addressing Long Term Benefits and Pension Obligations

Lizette Navarette, Vice President

Community College League of California

Questions To Frame This Session

- What long-term structural problems are with in my control to address?
- What policy advice do elected officials and administrators need to address pressure by public employees and their unions to continue often-unsustainable benefits?
- How can public employers balance the dilemma of unsustainable long-term costs and short-term demands for public services and stable employment relations?

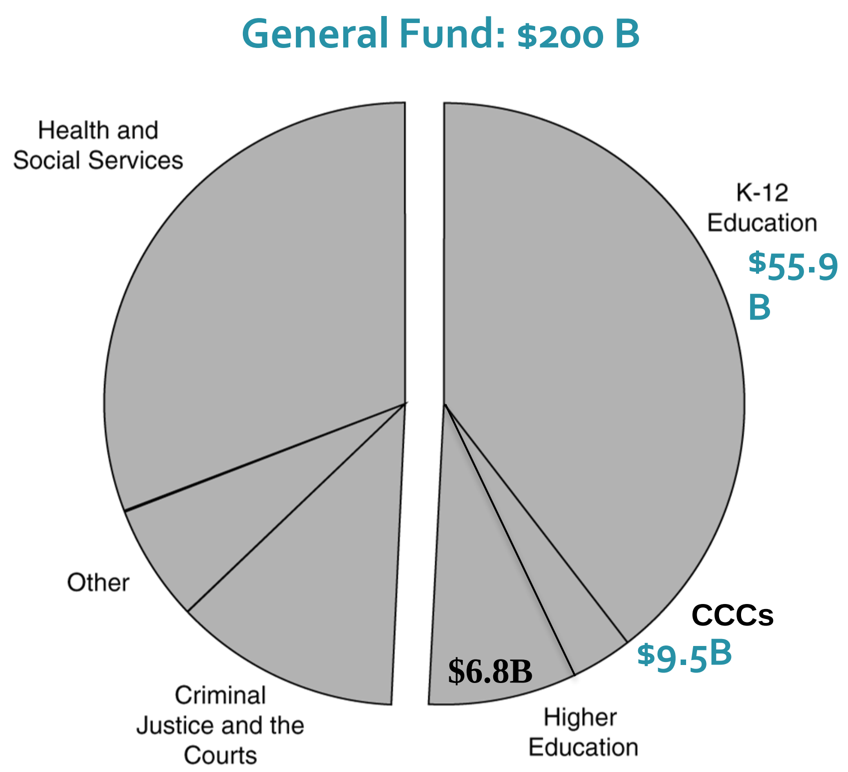
STRS & PERS Future Rates

Fiscal Year	STRS – Employer Rates	STRS – Employee Rates (Pre/Post PEPRA)	PERS – Employer Rates	PERS – Employee Rates (Pre/Post PEPRA)
2013-14	8.25%	8.00%	11.44%	7.00%/6.00%
2014-15	8.88%	8.15%	11.77%	7.00%/6.00%
2015-16	10.73%	9.20%/8.56%	11.85%	7.00%/6.00%
2016-17	12.58%	10.25%/9.205%	13.89%	7.00%/6.00%
2017-18	14.43%	10.25%/9.205%	15.53%*	7.00%/6.50%*
2018-19	16.28%	10.25%/10.205%	18.10%*	7.00%/6.50%
2019-20	18.13%	10.25%/10.205%	20.80%*	7.00%/6.50%
2020-21	19.10%	10.25%/10.205%	23.80%*	7.00%/6.50%
2021-22	18.6%	10.25%/10.205%	24.6%*	7.00%/6.50%

* Revised per 4/18/17 CalPERS Finance and Administration Committee agenda due to change in discount rate

Cost Pressures Throughout the Budget

Education makes up half of state spending.



Political Dynamics

What Problem?

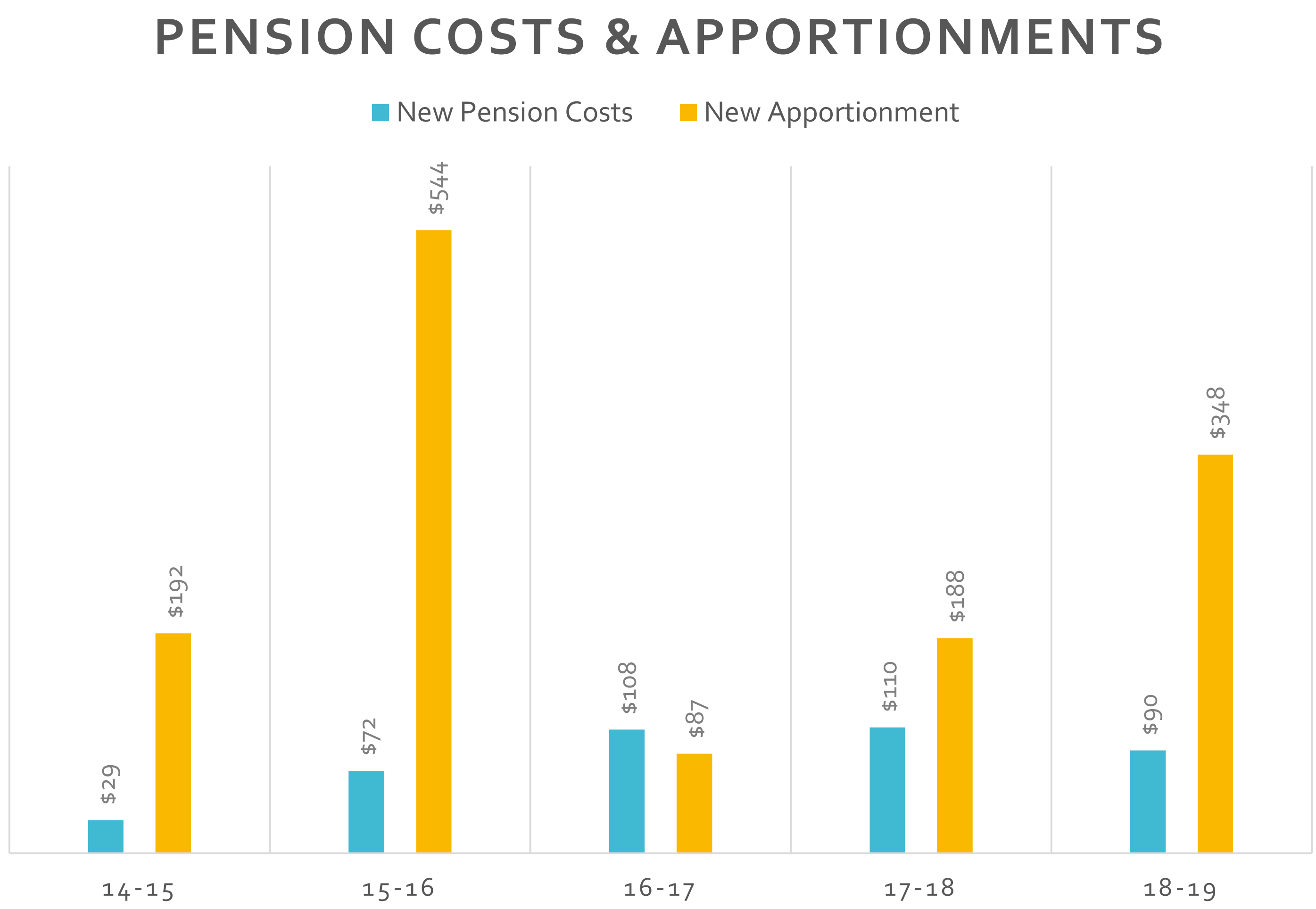
- Due to term-limits, mistakes of the past are vaguely understood by elected officials
- Many assumed the problem would resolve itself once the economy began recovering.
- Without an intimate understanding of local budgets, leaders don't see the depth of the problem.

We Gave You Resources…

- Legislator Perspectives
  - Base increase should be used to cover obligations
- Legislators reluctant to allocate general operating costs above pension increase
- Belief that we did this to ourselves.
- Concern with making new investment but getting nothing new in return.

Political choice - pay more into state pension and potentially crowding out other spending in the budget, or let funding levels drop and pushing costs into the future.

Limited Revenue Sources



Long-Term vs. Short-Term Strategies

Short-Term

- **Get the Costs and Make Them Visible in Public**
  - Evaluate actual revenue with ALL ongoing expenses
- **Provide Visual Representations**
  - Continue to make the case for base increase
- **Solve for the Long Term First**
  - Monitor the long-term fiscal health of districts
  - Annual Financial Report requires a plan

Long-Term vs. Short-Term Strategies

Long-Term

- **Establish a Defined-Contribution OPEB Benefit**
  - A tools available to public employers seeking to restructure their OPEB benefits is a defined contribution retiree health savings plan.
- **Pension Rate Stabilization Programs**
  - Irrevocable trust designed to prefund pension costs and help districts get ahead of rising STRS/PERS rate increases.
- **Consider Labor Relations**
  - Employees and their labor representatives must first be informed of the long-term true-cost trajectory.

OPTIONS TO ADDRESS RISING PENSION LIABILITIES

Maureen Toal

Senior Vice President, PARS

THREE OPTIONS TO ADDRESS PENSION LIABILITIES

1. Pay-as-you-go
2. Set aside reserve funds
3. Set up and prefund into trust

PENSION PREFUNDING VS RESERVE ACCOUNT

RESERVE ACCOUNT	TRUST
General fund investing restrictions	Govt. Code Section 53216
Fixed income investing only	Fixed Income or diversified investing
Investments not tailored for long term	Can be tailored for short or long term
Revocable	Irrevocable
Can be accessed for other uses	Dedicated solely to pension costs
Not free from creditors	Exclusive benefit/free from creditors
No corporate trustee	Corporate trustee to mitigate fiduciary risk

BEST PRACTICE – PREFUNDING

- PARS/CCLC offers the largest and fastest growing Section 115 trust for pension prefunding in CA and the nation

- IRS Private Letter Ruling now enables public agencies to reduce their unfunded pension liabilities by setting aside contributions for pension obligations into their own locally controlled Section 115 retirement trust

- Previously, the only way to reduce unfunded pension liability was to send additional contributions in excess of annual required contribution to PERS/STRS

- Since 2015, **over 200 CA agencies** (including approximately 16 CCD's) are prefunding pension liabilities, with many more entities considering adoption

BENEFITS OF PREFUNDING PENSION OBLIGATIONS

1. Addresses Long-Term Liability
2. Addresses GASB 68 Liability
3. Protects Assets from Diversion
4. Serves as a Rainy Day Fund
5. Stabilizes Pension Costs
6. Helps to Achieve Better Returns
7. Beneficial in Credit Rating & Accreditation

San Bernardino Community College District

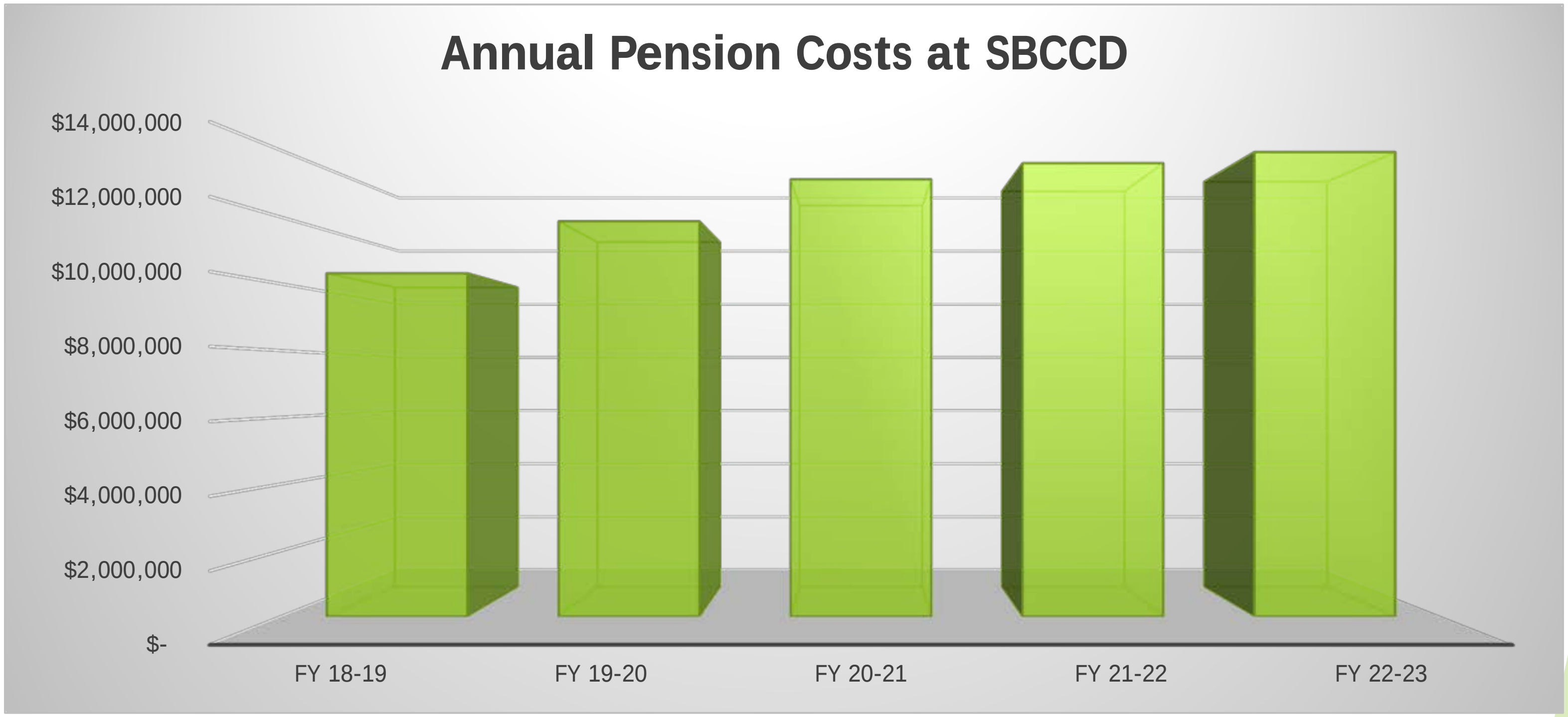
Jose Torres

Executive Vice Chancellor

SBCCD Agenda

1. Expected annual retirement costs for SBCCD
2. Why did SBCCD invest in Pension Rate Stabilization Trust (PRST) ?
3. Is it safe to invest in PRST?
4. PRST at SBCCD
5. Process at SBCCD to establish PRST
6. Questions to ask vendors

Expected Annual Retirement Costs for SBCCD



Why did SBCCD invest in Pension Rate Stabilization Trust (PRST)?

- To address increasing retirement benefit costs
- Found a way to invest excess funds with a higher than expected annual return rate
- Restricted investment policies
- Fixed income interest rate is low
- Flexibility
  - We can withdraw up to 2 years of retirement costs ($22m)
  - Then afterward, we can withdraw up to 1 year of retirement costs ($13m)
- Easy to track multiple sub-accounts
- Restricted for retirement costs?
  - Yes
  - Use General Fund and Other Funds for various purposes

Is it safe to invest in PRST?

- There are risks and investment is subject to market conditions
- PARS offers 4 different investment portfolios
  - Fixed Income (100% Fixed Income & 0% Equity)
  - Conservative (42% Fixed Income & 58% Equity)
  - Balance (60% Fixed Income & 40% Equity)
  - Growth (75% Fixed Income & 25% Equity)
- What’s the tolerance level of your board?
- Alternative is your County Treasurer or investment firm

PRST at SBCCD

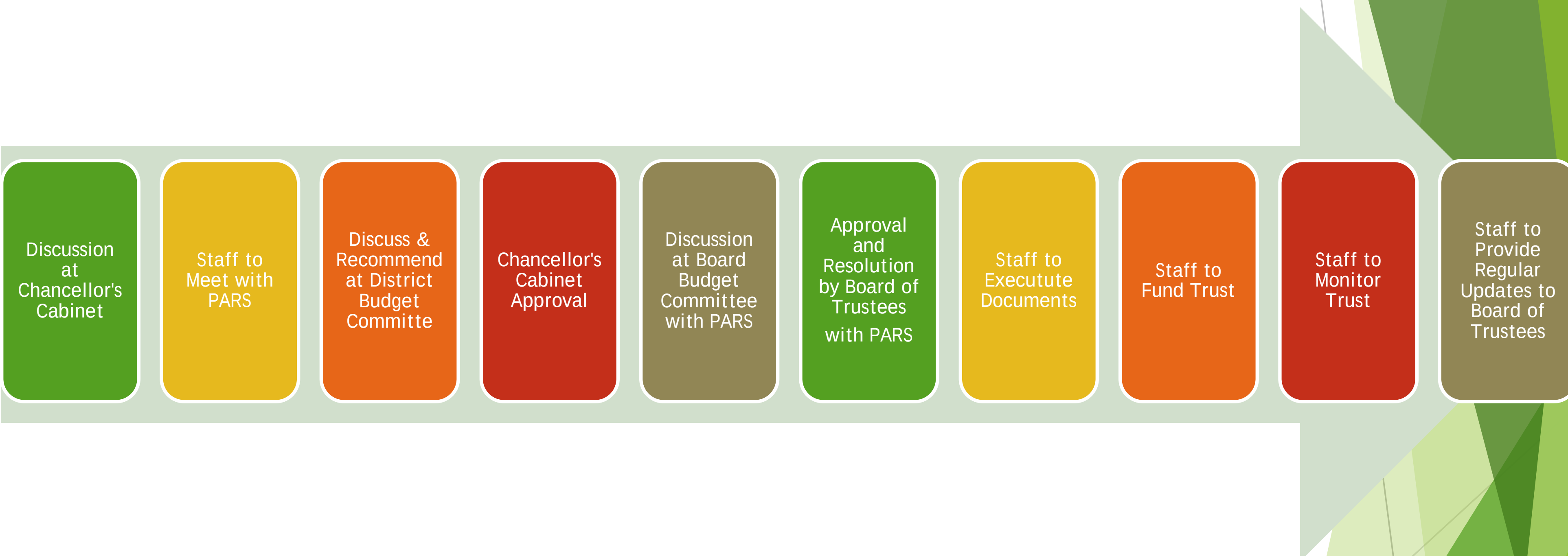
SBCCD Investment

- $75 million
  - 4 separate sub-accounts
    - $25 million – General Fund
    - $5 million - SBVC
    - $21 million - KVCR
    - $24 million - FCC

Annual Expected Rates of Return

- Conservative Portfolio
  - 3 years = 4.17%
    - $3.1 million based on $75 million
  - 5 years = 5.20%
    - $3.9 million based on $75 million
  - 10 years = 5.65%
    - $4.2 million based on $75 million

Process to Establish PRST at SBCCD



Questions to Ask Vendors

1. Who manages/administers the investments?
2. What are the investment options for the District?
3. What is the expected rate of return for each investment option?
4. How do these investment options compare with County Treasury Pool and/or LAIF?
5. Why is it that we can have different investment options from our own Investment Policies?
6. What are the fees?
7. Can we easily track various investments (subaccounts)?
8. How often do we receive statements? Please provide example of statement.
9. How often can the Board get a presentation on the investments?
10. How much can the District withdraw from the trust on an annual basis?
11. How often can the District withdraw funds from the trust?
12. What is the turnaround on withdrawals?

Cuesta College's Process

Dan Troy

Assistant Superintendent/Vice President Administrative Services, Cuesta College

How did we get here?

- 2014 — CalSTRS unfunded liability of $74 billion and CalPERS unfunded liability of $62 Billion
- AB 1469 enacted increases both employee and employer contribution rates – employer rates would grow from 8.25% to 19.1% in 2020-21
- Meanwhile the CalPERS Board has also implemented large increases – from 11.442% in 2013-14 to an estimated 25.7% in 2024-25
- These increased rates act like a negative cost-of-living-adjustment for districts, consuming larger amounts of budget expenditures

Cuesta College
Unrestricted GF Pension Costs

- 2013-14: $2.9 M
- 2018-19: $6.2M

- Pension costs have grown from 6.2% to 11.4% of GF expenditures

State Response

- State has provided resources to help
  - Unrestricted increases
  - One-time mandate reimbursement funds
- But…
  - This follows significant downturns in funding
  - Low or no COLAs
  - Direct funding reductions
  - Declining FTES

Addressing Pensions

- Communication
- Budget Assumptions
- Multi-year Projections
- Actions

Pension Rate Stabilization Program (PRSP)

- Board meeting information item
  - August 2017
- Participatory Governance
  - Committee Initiative
- Identify Resources
  - One-time funds
- Community buy-in
  - Unanimous recommendation from workgroup and full committee

Pension Rate Stabilization Program (PRSP)

- Recommendation to Board of Trustees –
  - Invest $3M of 1-time funds
  - Conservative Fund (4% target)
  - Review 1-time funds annually to consider additional investment

For Consideration

- PRSP alone will not solve problem
  - District has taken many other significant actions (Faculty SIP, hiring frost, etc.)
- Not like OPEB
  - Ongoing vs One-time cost
- Make right choice for your district